



United States Agency for International Development
Georgia Banking Infrastructure Development - II



FIRST YEAR WORK PLAN

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Submitted by
Chemonics International
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Chemonics International, on behalf of itself and its subcontractor, Bankworld Inc., is pleased to submit this work plan the First Year of Georgia Banking Infrastructure Development – II.

We look forward to serving USAID, the National Bank of Georgia and various other counterparts in the Republic of Georgia in meeting the objectives of the Task Order.

Should there be any question on the Plan, we would most welcome hearing.

WORK PLAN

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USAID
Georgia Banking Infrastructure Development – II
First Year Work Plan

Article 1. General Purpose and Nature of Assistance

This program is intended to assist the National Bank of Georgia (“NBG”) carry out its responsibility for ensuring the safety, soundness and stability of the commercial banking system in Georgia. In the process of implementing all necessary banking supervision reforms, the NBG will receive technical assistance to develop a proper accounting and legal framework to monitor and conduct the on-site and off-site inspections of the commercial banks.

The provisions for this in-kind assistance is subject to the terms and conditions of the Memorandum of Understanding (“MOU”) that was executed and signed on December 19, 1999 between the NBG and the United States Agency for International Development (“USAID”).

Article 2. Goals and Objectives

This work plan outlines the framework for mutual cooperation between the NBG and USAID to achieve the stated purpose outlined in Article 1 above.

2.1 On-Site Inspections. The goal is to provide the NBG with a standardized and comprehensive on-site inspection program that will allow the NBG’s supervisors and/or inspectors to evaluate the risk(s) at commercial banks using a common, standardized methodology of evaluating financial and operating risks. This assessment will result in a composite rating being assigned to each commercial bank using the CAMEL System.

The joint efforts between the NBG and USAID are detailed in the agreed benchmarks set out in Article 3 of this work plan but include the following areas.

- The continued development and refinement of an inspection program for the commercial banks utilizing the CAMEL system as the standard for performing on-site inspections;
- The continued implementation for using the inspection report as a management tool which effectively communicates a commercial bank’s strengths and weaknesses to the subject bank’s supervisory board;
- The continued development and refinement of a legal framework that will support the work of the supervisory department in adopting and implementing

the timely and appropriate actions needed to eliminate the commercial banks' violations of laws and regulations and other unsafe and unsound practices;

- The continued implementation of an inspector accreditation (training) program to sustain and institutionalize the overall supervision function will be developed and provided to the supervisory staff;
- The development of a working group consisting of the IMF, IFC, EBRD, World Bank, USAID, and other donors involved in the commercial banking system to enhance the communication process involving the various reforms being implemented between the various donors and the relevant participants.

2.2 Off-Site Analytic System. The goal is to ensure that the NBG has a reliable and adequate information network, utilizing data and information submitted by the commercial banks. The staff of the banking supervision department will use this information to monitor the commercial banks' financial condition for the purpose of identifying risks between on-site inspections.

The joint effort between the NBG and USAID are detailed in the agreed benchmarks set out in Article 3 of this work plan but include the following areas:

- An assessment of the commercial banks' ability to submit timely and accurate financial information (on a regular basis) to the NBG's Bank Supervision Department will be made, and recommendations for improvement will be made where appropriate.
- The further development and refinement of the off-site surveillance system ("UBPR"), which will assist in the identification of potential problems at commercial banks between the regularly scheduled inspections, will be performed.
- The continued development and refinement of CAEL reporting format, focusing on an Executive Summary for BSD and NBG senior management.
- The continued refinement and updating of the "Off-site Inspection Manual".
- An integrated approach to linking the on-site and off-site program will be refined, as it is critical to ensure that all pertinent supervisory information concerning a commercial banks activity is shared between these two areas.

2.3 Bank Consolidation and Problem Bank Resolution. The goal is to improve the current program and methodology by the NBG for affecting the resolution of problem banks, including procedures utilizing any new expanded enforcement powers that have been provided under the new laws and regulations that are currently being developed and implemented.

The joint effort between the NBG and USAID are detailed in the agreed benchmarks set out in Article 3 of this work plan and include the following areas.

- Determine which banks present the most financial risk to the banking system and then develop a plan to minimize the cost of resolving the problems without increasing the risk to the entire banking system.
- Continued assistance for the Bank Supervision Department to help implement measures and procedures directed at rehabilitation rather than liquidation of troubled banks.
- The refinement of a system of Supervisory Action Plan to be implemented by the supervisory staff of the NBG when a commercial bank becomes a "problem bank" as defined by the NBG.
- Develop a NBG policy to coordinate the transfer of responsibility for the liquidation of problem and/or insolvent banks when they are declared insolvent or upon the revocation of the bank's license.

2.4 Legal Strengthening

The following tasks with regard to the Legal Component of the Project will be completed, as detailed below. Subsection 3.1.4 of this work plan provides the Plan Delivery Dates for each task.

A - Legislative

The goal will be to supplement the Legislative Program results achieved under Phase I by performing the following tasks.

- Recommending, drafting and analyzing with the NBG several brief but important proposals to again amend the “Commercial Banking Law” to improve the definition of “Subsidiary”; to confer on the NBG the right to pre-approve all banks’ External Auditors on a case by case basis and to expressly provide for civil money penalties against bank administrators to implement the new authority, obtained under the amended “Organic Law on the National Bank,” to assess fines against individuals.
- Assisting the NBG in its lobbying efforts in the Parliament with respect to the critical amendments to the “Commercial Banking Law”, delivered to the NBG during Phase I and since submitted to Parliament, which provide for the extension of fit and proper criteria to the members of banks’ Supervisory Councils and significant owners and which also require prior NBG permission for changes in the control of a bank.

- Recommending, drafting and analyzing with the NBG several brief but critical proposals to amend the “Criminal Code” by adding a new subsection to the “Financial Crimes” section. The new subsection, to be titled “Bank Crimes”, would criminalize serious abuse of banks and other depositary institutions by insiders and their confederates. It would provide for a range of punishments in the form of heavy fines and/or imprisonment for those convicted of bank asset stripping, bank defalcation and other types of felonious larceny from banks as well as false financial reporting and other devices to conceal criminal acts at banks.
- Recommending, drafting and analyzing with the NBG proposals to amend the “Administrative Violations Code” to punish compliance violations less virulent than criminal and abusive practices and which have less serious consequences for depositors.

B - Regulatory

The goal will be to complete the Regulatory Program objectives planned and achieved under Phase I by performing the following tasks.

- To work with the NBG to expedite the internal processing and near-term issuance of regulations on capital, fit and proper managers, foreign exchange, fixed assets, credit concentrations and large exposures, and general accounting principles which have all been delivered to the NBG during Phase I.
- To recommend, draft and analyze with the NBG new regulations covering bank supervisory councils’ governance, corrective actions, holding companies, civil sanctions, liquidity, securities activities, licensing, branching and mergers.

C - Transactional

- The goal will be to increase legal advice and support to the NBG in matters involving decision-making in distressed bank situations. This increase will serve to take up the duties, as needed, of the specialist Advisors to the NBG who are no longer available to recommend and counsel senior NBG officials, particularly in the areas of “Temporary Administrations (Conservatorships)” and Bank Liquidations.

D - Judicial

- The goal will be to participate in the ABA/CEELI, World Bank funded Judicial Training Program at the Judicial Training Center in Tbilisi.

Participation will consist of planning and teaching Georgian judges from all trial and appeal courts. The teaching will be done by the Project's local lawyer (who functions as Supervisory Counsel to the NBG) under the guidance of the Project's Senior Legal Advisor who will work closely with USAID in lecture planning and execution.

E - Legal Training at the NBG

- The goal will be to train the senior and junior supervisory and examination staff members at the NBG in the knowledge and application of the new powers now available to them under the banking law amendments achieved under Phase I of the Project. Case studies in strategies and tactics for situations involving troubled and distressed banks will be emphasized, as will be other important new concepts and tools. Here, the training will cover investigations of persons who propose to control banks and of their proposed sources of capital, and will include the proper judgments processes in the application of fit and proper standards for bank administrators.

2.5 Accounting Procedures Strengthening. The goal is the adoption of international accounting, and reporting standards, by all licensed commercial banks. Requirements stipulated in supervisory and regulatory pronouncements of the NBG will be based on approved international accounting standards and practices.

The joint efforts between the NBG and USAID are detailed in the agreed benchmarks set out in Article 3 of this work plan but include the following areas.

- The continued development of an accounting methodology unit supporting the Bank Supervision Department of the NBG.
- The development of accounting policy positions and regulations that support the adoption of newly approved IFRS Chart of Accounts and accounting practices consistent with International Financial Reporting Standards (IFRS).
- Assistance and advice to the NBG on formulating responses to inquiries on accounting issues from commercial banks and the NBG's Bank Supervision Department.
- The continued development of a management reporting system to enhance the risk management capability of the commercial banks.
- Training to commercial banks accounting staff and bank supervision staff on specific accounting topics including external and internal audit programs.

- The completion of an internal audit program and promotional support towards its adoption by commercial banks.

Article 3. Benchmarks

3.1 The Goals and Objectives of this work plan will be implemented as detailed in the following timeframes.

3.1.1 On-Site Inspections. The Parties shall achieve the following benchmarks with regard to On-Site Supervision:

- A review of the duties and objectives of the On-Site Inspection Division will be continued to determine if the present management structure and staffing is adequate given the present workload requirements.

Timeframe for Implementation: June /July 2002

- 10 inspections, in which the Resident Advisor will be involved on site at the commercial banks, will be performed during the next 12 months. These 10 inspections (in which the resident advisor will participate) will only involve large banks as ranked by assets or those banks that have systemic risk to the banking sector or other unusual operating problems requiring unique assistance. These 10 inspections will require that the reports be translated into English and a formal review process by the Resident Advisor(s) will be performed at the conclusion of each inspection. These review sessions will include written comments and suggestions to be presented in a workshop format to discuss the recently completed inspections.

Timeframe for Implementation: Beginning May 2002 and continuing through May 2003

- The current on-site inspection procedures will be revised to increase their effectiveness and to ensure that all new laws and regulations recently adopted are addressed during an on-site inspection. The additional items for review and consideration involve the commercial bank's adherence and compliance with the newly implemented International Accounting Standards, new asset classification procedures, new internal auditing procedures, new conflicts of interest procedures, and new rules regarding corporate governance procedures for the supervisory councils of commercial banks.

Timeframe for Implementation: June - August 2002

- The inspection manual currently in use by the on-site inspection staff will be reviewed and updated to ensure that the new laws and regulations are adequately addressed. In addition, training sessions will be conducted to explain the practical aspects of the new regulations to the supervisory staff.

Timeframe for Implementation: August 2002

- An Accreditation Program for the banking supervision staff will continue to be implemented. The 5th course will be presented in the summer of 2002. These courses are intended to ensure that the staff has the basic skills necessary to carry out the regulatory objectives and procedures of the NBG.

Timeframe for Implementation: July/August 2002

3.1.2 Off-Site Analytic System. The Parties shall achieve the following benchmarks with regard to Off-Site Supervision:

- A review of the duties and objectives of the Off-Site Inspection Division will be continued to determine if the present management structure and staffing is adequate given the present workload requirements.

Timeframe for Implementation: June 2002

- Conduct a seminar on how to use the UBPR as an analytical tool to assess strengths and weaknesses of individual banks. The seminar will be supplemented by spending a day with each off-site inspector, providing individual instruction on the UBPR and new CAEL format. Instruction will be focused on the 8 to 10 largest Georgian banks.

Timeframe for Implementation: June/July 2002

- Update and refine CAEL reporting format, focusing on an Executive Summary for BSD and NBG senior management.

Timeframe for Implementation: June/July 2002

- Refine and update “Off-Site Inspection Manual,” incorporating the newly developed “UBPR”.

Timeframe for Implementation: July – August 2002

- Develop Instruction Manual for UBPR. Manual will focus on detailing the input information for the ratios. The manual will also provide some guidance on how to interpret the information.

Timeframe for Implementation: August 2002

- Continued individual assistance and instruction on these new tools and procedures will be provided to the Off-Site Division and its inspectors throughout the year.

3.1.3 Bank Consolidation and Problem Bank Resolution. The Parties shall achieve the following benchmarks with regard to resolving problem banks.

- Review the existing Regulation No. 263 "System for Supervisory Actions of the Activity of Commercial Banks" to determine whether it serves the purpose of taking timely, appropriate, and effective corrective action on banks facing potential difficulties. If necessary, this regulation will be combined or incorporated in a new regulation on prompt corrective action to allow the NBG to have the necessary tools to correct problem situations before the trust of the depositors and other creditors decreases and the bank's financial condition deteriorates further.

Timeframe for Implementation: July 2002

- Identify each institution that is not reporting compliance with the applicable capital regulation or has a composite CAMEL rating of 4 or 5.

Timeframe for Implementation: June 2002

- Implement supervisory and enforcement action where applicable (e.g. targeted inspections, remedial agreements, memoranda of understanding, cease and desist order, temporary administrators, etc.) for those commercial banks that are not meeting the minimum capital requirement or those that have a composite rating of 4 or 5.

Timeframe for Implementation: Beginning May 2002 and continuing throughout the year.

- Develop and implement an early intervention program, which entails various strategies for the merger of several troubled banks with financially healthy and strong banks.

Timeframe for Implementation: Beginning in July 2002 and continuing throughout the year

- Development and implementation of a guidance manual for Temporary Administrators.

Timeframe for Implementation: August – October 2002

3.1.4 Legal Strengthening. The parties shall achieve the following benchmarks with regard to the following elements of legislative and regulatory reforms, and transactional and judicial assistance.

A. Legislative Tasks

- Amendments to the Commercial Banking Law. These amendments will redefine “Subsidiary” to make it more comprehensive to strengthen the power of the NBG and will require External Auditors to be approved by the NBG.

Timeframe for Implementation: May 2002

- Assisting the NBG with its lobbying efforts with respect to the amendments to the Commercial Banking Law which were delivered during Phase I of the Project

Timeframe for Implementation: June 2002

- Amendments to the Criminal Code. This amendment will add a new Bank Crimes section criminalizing serious insider abuse and theft by individuals as well as and taking deposits without a license. It will provide a range of punishments including heavy fines and imprisonment for offenders.

Timeframe for Implementation: June 2002

- Amendments to the Administrative Violations Code. These amendments will add provisions providing fines against individuals for serious compliance violations such as licensing violations, false reporting and disobeying or ignoring NBG regulations and instructions.

Timeframe for Implementation: June 2002

B- Regulatory Tasks

The issuance of six all previously delivered and analyzed regulations. All are to be issued by September 2002 and include the following:

- Regulation on Credit Concentration
- Regulation on Fixed Asset Limitations
- Regulation on International Accounting Principals
- Regulation on Foreign Exchange Management and Limitations
- Regulation on Capital Requirements
- Regulation on Fit and Proper Criteria for Bank Managements

The following regulations are listed in priority order based on the need to start or complete design work and discussion on several of them sooner rather than later. But the Delivery Dates shown do not necessarily appear in chronological order due to the variances in anticipated time devoted to drafting, analysis and discussion with the NBG before actually delivery.

- Regulation on Fiduciary Duties of Bank Supervisory Councils

Timeframe for Delivery to NBG: July 2002

- Regulation on Prompt Corrective Actions

Timeframe for Delivery to NBG July 2002

- Companies and Other Persons Who Control Banks

Timeframe for Delivery to NBG: June 2002

- Regulation on Liquidity Management

Timeframe for Delivery to NBG: June 2002

- Regulation on Sanctions and Penalties

Timeframe for Delivery to NBG: July 2002

- Regulation on Securities Activities of Bank Subsidiaries

Timeframe for Delivery to NBG: July 2002

- Regulation on Mergers

Timeframe for Delivery to NBG: August 2002

- Regulation on Licensing and Branching

Timeframe for Delivery to NBG: September 2002

3.1.5 Accounting Procedures Strengthening: The parties shall achieve the following benchmarks with regard to accounting issues:

- Assist the staff of the AMD to develop and implement a program to monitor the commercial bank's progress in the completion process of their external audits. This process includes the analysis of all recommended audit adjustments and to ensure the commercial banks actually book the adjustments.

Timeframe for Implementation: May – July 2002

- Working with the staff of the AMD, the list of revisions to the Chart of Accounts that were developed during Phase I will be finalized and approved by the NBG.

Timeframe for Implementation: June – August 2002

- Assist the staff of the AMD with a quarterly review of the largest bank's accounting data that is submitted to the NBG quarterly. An assessment will be made of this accounting information using a software program, which is intended to highlight potential problems and irregularities

Timeframe for Implementation: Beginning in July 2002 and continuing each quarter thereafter.

- The accounting regulations and position papers that were developed during Phase I of the project will be finalized with the NBG staff and completed for final implementation.

Timeframe for Implementation: June – September 2002

- During the on-site inspection process the accounting advisors will provide on the job assistance in the analysis and review of accounting related matters and the development of related report comments.

Timeframe for Implementation: Beginning in June 2002 and continuing until April 2003

- As requested and the situation warrants, the local accounting staff, will provide written opinions and analysis regarding accounting issues to

the accounting methodology department and to the accounting staff of the commercial banks.

Timeframe from Implementation: Beginning in June 2002 and continuing until April 2003

- Assist selected commercial banks in developing the internal audit function. Assess the progress of development of internal audit function and provide recommendations and on-site direct assistance. Consultancy may include but is not limited to: mandatory usage of internal audit manual, developing internal audit reports, organizing working papers and filing system.

Timeframe for Implementation: August 2002 and on-going

- Continue to provide assistance through the help-desk to the commercial banks on the inquiries related to accounting issues. Identify frequently asked questions and on monthly basis issue questions and answers papers and provide them to all commercial banks

Timeframe for Implementation: June 2002 and on going

4 – Selected Topics for Seminars/Presentations

- Presentation on External Audits

Timeframe for Implementation: May 2002

- Seminar on the newly passed Banking Laws and Regulations and on Supervisory and Regulatory Policies will be provided.

Timeframe for Implementation: July 2002

- The 5th course of the accreditation program, a computer simulation for banking operations will be presented to the inspectors.

Timeframe for Implementation: July/August 2002

- A one-week training program on ratio analysis, utilizing the information provided by the UBPR will be developed. The training will be provided by an FSVC volunteer and will focus on trend, peer comparisons and ranking. The training will also focus on the interrelationships of the balance sheet and income statement, and identifying the reasons behind the trends.

Timeframe for Implementation: August/September 2002

- Conduct US based training with a US bank regulatory agency for 5-6 members of the NBG's on-site supervisory staff.

Timeframe for Implementation: October 2002

- Conduct two multi-day training seminars for the commercial banks on IFRS concepts and related issues based on inquiries and frequently asked questions by the commercial banks;

Timeframe for Implementation: September 2002 and March 2003